

1 WAYNE STRUMPFER  
 Acting California Corporations Commissioner  
 2 ALAN S. WEINGER (CA BAR NO. 86717)  
 Acting Deputy Commissioner  
 3 NICHOLAS LANZA (CA BAR NO. 124721)  
 Senior Corporations Counsel  
 4 DEPARTMENT OF CORPORATIONS  
 320 West 4<sup>th</sup> Street, Suite 750  
 5 Los Angeles, California 90013-2344  
 Telephone: 1 (888) 877-5379, ask for: (213) 576-7189  
 6 Attorneys for Complainant

7  
 8 BEFORE THE DEPARTMENT OF CORPORATIONS  
 9 OF THE STATE OF CALIFORNIA  
 10

11 In the Matter of	) FILE NO. 112566
	)
12 THE CALIFORNIA CORPORATIONS	) STATEMENT IN SUPPORT OF ORDER
13 COMMISSIONER,	) LEVYING ADMINISTRATIVE PENALTIES
	) PURSUANT TO CORPORATIONS CODE
	) SECTION 25252
14 Complainant,	)
	)
15 v.	)
	)
16 PALISADES INVESTMENT ADVISORS,	)
17 INC.,	)
	)
18 Respondent.	)

19  
 20 Wayne Strumpf, the Acting California Corporations Commissioner ("Commissioner") of  
 21 the Department of Corporations ("Department") alleges and charges as follows:

- 22 1. Palisades Investment Advisors, Inc. ("Palisades") holds a valid and unrevoked  
 23 investment adviser certificate issued by the Commissioner on August 19, 1999, pursuant to  
 24 Corporations Code section 25230. Palisades is an investment adviser business located at 11601  
 25 Wilshire Blvd., Suite 2460, Los Angeles, California 90025. Palisades is a California corporation.  
 26 Mr. Stephen J. Hoshimi ("Hoshimi") is Palisades' president and chief executive officer.  
 27 2. On or about February 17, 2004, the Commissioner commenced a regulatory  
 28 examination of Palisades. The examination and subsequent follow-up inquiries revealed violations

1 of regulations promulgated pursuant to the Corporate Securities Law of 1968 (Corp. Code § 25000 et  
2 seq.).

3 3. These violations included Palisades' failure to meet net capital requirements (Cal. Code  
4 Regs., title 10, § 260.237.1, subd. (a).), and its failure to make and keep general and auxiliary ledgers  
5 (Cal. Code Regs., title 10, § 260.241.3, subd. (a)(2).). The books and records requirements provide  
6 the Department with a regulatory mechanism to protect the public by validating the investment  
7 adviser licensee's liquidity and financial integrity on a monthly and yearly basis. Palisades' failure  
8 to meet its books and records requirements prevented the Department from determining, at the time  
9 of its regulatory examination, if Palisades met the capital requirements imposed by the Corporate  
10 Securities Law and the regulations enacted thereunder.

11 4. Corporations Code section 25241 provides that investment advisers are required to  
12 maintain books and records that are subject to examination by, and to file such reports as required  
13 by, the Commissioner. Corporations Code section 25241 provides, in relevant part, as follows:

14 [E]very investment adviser licensed under Section 25230 shall make and keep  
15 accounts, correspondence, memorandums, papers, books, and other records and shall file  
16 financial and other reports as the commissioner by rule requires....

17 5. California Code of Regulations, title 10, section 260.241.3 requires that investment  
18 advisers maintain specific books and records. Subdivision (a)(2) of section 260.241.3 provides as  
19 follows:

20 (a) Every licensed investment adviser shall make and keep true, accurate and current the  
21 following books and records relating to such person's investment advisory business:

22 (2) General and auxiliary ledgers (or other comparable records) reflecting asset, liability,  
23 reserve, capital, income and expense accounts.

24 6. Prior to April 3, 2003, California Code of Regulations, title 10, section 260.237.1  
25 contained the capital requirements for investment advisers. Subdivision (a)(2) of section 260.237.1  
26 provided, in relevant part, as follows:

27 (a) No investment adviser who has any power of attorney from any investment advisory  
28 client to execute transactions . . . shall permit its total aggregate indebtedness to exceed 500%

of its tangible net capital or permit its current aggregate indebtedness to exceed its current net capital; and,

...

(2) If the investment adviser has any power of attorney from any investment advisory client to execute transactions and does not have regular or periodic custody or possession of any of its investment advisory clients' securities or funds, except the receipt of prepaid subscriptions for periodic publications, or other investment advisory services, it shall at all times have and maintain tangible net capital of not less than \$5,000....

Subdivision (c) of section 260.237.1 provided that for purposes of section 260.237.1, subdivision (a), all financial information be determined in accordance with generally accepted accounting principles.

7. On April 3, 2003, California Code of Regulations, title 10, section 260.237.1, subdivision (a)(2) was amended to read as follows:

An investment adviser licensed prior to 03/01/03 may comply with either the minimum financial requirements in this section or in Section 260.237.2 until January 1, 2005, at which time this section shall become inoperative and an investment adviser shall comply with the minimum financial requirements in Section 260.237.2.

(a) No investment adviser who has any power of attorney from any investment advisory client to execute transactions. . . shall permit its total aggregate indebtedness to exceed 500% of its tangible net capital or permit its current aggregate indebtedness to exceed its current net capital; and,

...

(2) If the investment adviser has any power of attorney from any investment advisory client to execute transactions and does not have regular or periodic custody or possession of any of its investment advisory clients' securities or funds, except the receipt of prepaid subscriptions for periodic publications, or other investment advisory services, it shall at all times have and maintain tangible net capital of not less than \$5,000;

8. On April 3, 2003, California Code of Regulations, title 10, section 260.237.2, subdivision (a) was added, and reads as follows:

An investment adviser licensed prior to 03/01/03 may comply with either the minimum financial requirements in this section or in Section 260.237.1 until January 1, 2005, at which time Section 260.237.1 shall become inoperative and an investment adviser shall comply with the minimum financial requirements in this section.

(a) Every investment adviser who has custody of client funds or securities shall maintain at all times a minimum net worth of \$35,000, and every investment adviser who has discretionary authority over client funds or securities but does not have custody of client

1 funds or securities, shall maintain at all times a minimum net worth of \$10,000.

2 9. The Department's examiner found during the regulatory exam on February 17, 2004,  
3 that Palisades had discretionary authority and power of attorney to execute transactions in the  
4 brokerage accounts of its investment adviser clients. Therefore, Palisades was required to meet either  
5 the net capital requirements provided for under section 260.237.1, subdivision (a), or the minimum  
6 net worth requirement provided for under section 260.237.2, subdivision (a).

7 10. At the time of the February 17, 2004 examination, Palisades had not maintained a  
8 general ledger accounting system, in violation of California Code of Regulations, title 10, section  
9 260.241.3, subdivision (a)(2). As a result of Palisades' violation, the Department's examiner was  
10 unable to determine if Palisades, at the time of the examination, was in compliance with either the  
11 net capital requirements of section 260.237.1, or the minimum net worth requirement of section  
12 260.237.2.

13 11. On April 20, 2004, the Department sent Hoshimi a regulatory letter explaining the  
14 violations discovered during the February 17, 2004 examination. On April 30, 2004, Hoshimi  
15 responded by letter, stating in part that the books and records requirements were not met because he  
16 thought they were only required for the Department's 2000 audit. He also stated that Palisades  
17 would comply with the capital requirement of section 260.237.1, until that section became  
18 ineffective on January 1, 2005. Hoshimi also submitted a trial balance sheet for March 31, 2004 and  
19 annual financial reports for 2000, 2001, 2002 and 2003.

20 12. However, after reviewing the trial balance sheet and the annual financial reports, the  
21 Department informed Hoshimi by letter dated November 3, 2004, that it had determined that  
22 Palisades had both tangible net capital and current net capital deficiencies for March 31, 2004 and  
23 for the years 2000, 2001, 2002 and 2003, in violation of California Code of Regulations, title 10,  
24 section 260.237.1, subdivision (a). The Department also directed Palisades to begin submitting  
25 monthly interim reports reflecting compliance with the net capital requirements.

26 13. A prior regulatory examination of Palisades in July 2000 also revealed record keeping  
27 and reporting violations, in the form of failure to meet net capital requirements (Cal. Code Regs.,  
28 title 10, § 260.237.1, subd. (a).), and failure to make and keep general and auxiliary ledgers (Cal.

1 Code Regs., title 10, § 260.241.3, subd. (a)(2).). In correspondence between the Department and  
2 Hoshimi during 2000, Palisades was put on notice of these violations. Hoshimi acknowledged  
3 receiving the letters notifying him of the violations.

4 14. Corporations Code section 25252, which became effective January 1, 1999,  
5 authorizes the Commissioner to issue an order levying administrative penalties against any  
6 investment adviser for willful violations of any provision of the Corporate Securities Law and any  
7 rules promulgated thereunder. Specifically, Corporations Code section 25252 provides, in relevant  
8 part:

9 The Commissioner may, after appropriate notice and opportunity for hearing, by orders, levy  
10 administrative penalties as follows:

11 ...

12 (b) Any broker-dealer or investment adviser that willfully violates any provision of this  
13 division to which it is subject, or that willfully violates any rule or order adopted or issued  
14 pursuant to this division and to which it is subject, is liable for administrative penalties of not  
15 more than five thousand dollars (\$5,000) for the first violation, not more than ten thousand  
16 dollars (\$10,000) for the second violation, and not more than fifteen thousand dollars  
17 (\$15,000) for each subsequent violation.

18 15. By reason of the foregoing, Palisades has willfully violated California Code of  
19 Regulations, title 10, section 260.237.1, subdivision (a) and section 260.241.3, subdivision (a)(2),  
20 justifying the imposition of administrative penalties. Palisades as a licensee, was obligated to have  
21 knowledge of, and to comply with, the provisions of the Corporate Securities Law and the  
22 regulations thereunder to maintain its investment adviser certificate. The Department gave Palisades  
23 prior notice of the requirements of both sections after its regulatory examination in 2000. Despite  
24 this, Palisades continued to violate both sections.

25 16. Therefore, pursuant to Corporations Code section 25252, the Commissioner seeks  
26 administrative penalties for Palisades' willful violations of the Corporate Securities Law of 1968 and  
27 the regulations adopted pursuant to it.

28 WHEREFORE, good cause showing, and pursuant to Corporations Code section 25252, the  
California Corporations Commissioner prays for an order levying administrative penalties in the  
amounts as follows, for willful violations of the following sections of title 10 of the California Code  
of Regulations: section 260.237.1, subdivision (a)--\$750.00, and section 260.241.3, subdivision

(a)(2)--\$750.00, for a total of \$1,500.00.

Dated: February 9, 2006

WAYNE STRUMPFER  
California Corporations Commissioner

By: \_\_\_\_\_  
NICHOLAS LANZA  
Senior Corporations Counsel  
Enforcement Division